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IN THE

Supreme Court of the United States

FILED
MAY 4 1967
JOHN F. DAVIS, CLERK

October Term, 1966

No. ~~1354~~ 127

READING COMPANY, *Petitioner*

v.

FRANCIS SHUNK BROWN, 3RD, *Trustee of the Estate of* I. J. KNIGHT REALTY CORP., *Bankrupt, Respondent*

and

UNITED STATES OF AMERICA, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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and

UNITED STATES OF AMERICA, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Petitioner prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered in the above-entitled case on January 6, 1967.

CITATIONS TO OPINION BELOW

The memorandum opinion of the Referee in Bankruptcy, which is unreported, and the opinion of the District Court, reported at 242 F. Supp. 337 (E.D. Pa., 1965), are contained in the record used below, nine copies of which are filed herewith in accordance with Rule 23(i). Both the majority and dissenting opinions of the Court of Appeals, which are not yet reported, are printed in Appendix C, hereto, *infra*, pp. 11-17.

JURISDICTION

The judgment of the Court of Appeals affirming the judgment of the District Court was entered on January 6, 1967. Rehearing was denied on February 13, 1967. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

QUESTIONS PRESENTED

May persons whose property has been destroyed or damaged by a fire caused by the negligence of a Federal Receiver in a bankruptcy proceeding recover their damages as an expense of administration of the estate, or are they without any remedy whatever against the Receiver and the Estate he represents?

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The pertinent constitutional provision is the Due Process clause of the Fifth Amendment to the United States Constitution, U.S.C. Const. Amend. V., Appendix A, *infra*, p. 8.

The pertinent statutory provisions are Sections 2, 62(a)-(1), 63(a)(7) and 64(a)(1) of the Bankruptcy Act, 11 U.S.C. §§11, 102(a)(1), 103(a)(7) and 104(a)(1)—all printed in Appendix B, *infra*, pp. 9-11, and 28 U.S.C. §959(a) and (b), *infra*, pp. 4-5.

STATEMENT OF THE CASE

On January 1, 1963, an eight-story industrial building located at 10th and Diamond Streets, Philadelphia, Pennsylvania caught fire and burned out of control for several hours causing millions of dollars worth of damage to adjoining property owners including the Reading Company. The building was under the control of a Federal Receiver who had been appointed by a District Court judge pursuant to a voluntary Petition for Arrangement under Chapter XI of the Bankruptcy Act filed by the owner, I. J. Knight Realty Company. It is admitted for the purposes of this

appeal that the fire was caused entirely by the negligence of a night watchman employed by the Receiver. The Reading Company filed a proof of claim for its damages and asked that it be allowed as an administrative expense entitled to priority over general claims. The Referee thereafter ruled that this claim should constitute a test suit and all persons damaged as a result of the fire would be bound by the result. The Trustee in Bankruptcy filed a motion to expunge the claim entirely, not only as an expense of administration, but also as an unsecured general claim. Referee Thomas J. Curtin granted the motion and the United States District Court for the Eastern District of Pennsylvania affirmed. The Court of Appeals affirmed the decision of the District Court in a 4-3 decision. The effect of the ruling is to deprive injured property owners of any redress whatever and to render a Trustee in Bankruptcy and the fund he administers immune from the consequences of his negligence. There is of course no difference, other than procedural, between bringing of an action for damages against the Trustee under 28 U.S.C. §959 and the filing of a proof of claim as was done here. In either case the claim would be subject to proof in the Bankruptcy Court. Under the ruling of the Court below neither the claim, nor a suit based upon the claim, would have any standing whatever against the fund.

The Receiver was appointed pursuant to a petition filed under Chapter XI of the Bankruptcy Act, 11 U.S.C. §701-99. The priority of the payment of debts under that Chapter is governed by Sections 62 and 64 of the Bankruptcy Act, 11 U.S.C. §102 and §104 which give first priority to "costs and expenses of administration," among other things.

The United States of America is named as a respondent herein because it opposed petitioner below. The United States has filed a federal tax claim against the Estate which would not be paid, if petitioner's position is sustained, because of the insufficiency of the Estate.

REASONS FOR GRANTING WRIT

1. The construction of the Bankruptcy Act adopted by the Court below is violative of due process. Permitting a receiver administering a fund owned by a class of creditors to destroy the property of another tortiously, with complete immunity given to the fund, is so arbitrary and unreasonable that it violates the Due Process clause of the Fifth Amendment of the United States Constitution. This Court has held that Congress may affect property rights under the Bankruptcy Act but must not transgress the bounds of due process. *Wright v. Union Central Life Ins. Co.*, 304 U.S. 502 (1938); *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935).

Petitioner's research has discovered no case in all of Anglo-American jurisprudence holding that a business being operated for the benefit of private economic interests is immune from liability for torts committed by the operator of the business. All decided cases, texts and authorities hold that, under general equity rules, torts committed by a receiver are not only provable but are invariably to be given priority status as costs and expenses of administration. See, *e.g.*, *Hale v. Frost*, 99 U.S. 389 (1878).

2. The decision of the Court of Appeals granting immunity from tort liability to a bankrupt estate completely nullifies that section of the Judicial Code (28 U.S.C. §959) which provides that trustees and receivers operating businesses are subject to suit to the same extent as private persons. That section reads as follows:

> "§959(a) Trustees, receivers or managers of any property, including debtors in possession, may be sued, without leave of the court appointing them, with respect to any of their acts or transactions in carrying on business connected with such property. Such actions shall be subject to the general equity power of such

court so far as the same may be necessary to the ends of justice, but this shall not deprive a litigant of his right to trial by jury.

"(b) A trustee, receiver, or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof. June 25, 1948, c. 646, 62 Stat. 926."

The right to sue a receiver, or any other tortfeasor, is obviously a nullity if the tortfeasor cannot be made to pay a judgment recovered in such a suit. Since a receiver or trustee is liable only in his representative capacity, *McNulta v. Lochridge*, 141 U.S. 327 (1891), the grant of immunity to the fund would render meaningless the right to sue granted by the above section. In that case, this Court said at 332:

"Actions against the receiver are in law actions against the receivership, or the funds in the hands of the receiver, and his contracts, malfeasances, negligences and liabilities are official and not personal, and judgments against him as receiver are payable only from the funds in his hands."

3. If the decision below prevails, receivers conducting businesses will fear to carry liability insurance sufficient to protect the public against substantial claims, much less disasters such as the fire which gave rise to this litigation. Under the holding there is no need to carry any insurance, and the dictum warns that any receiver paying "excessive" insurance premiums will be surcharged. (*infra*, appendix C, p. 17).

4. The decision is in conflict with prior decisions of this Court requiring,

(a) construction of the Bankruptcy Act in accordance wtih equity jurisprudence. *Pepper v. Litton*, 308 U.S. 295, (1939); *Securities and Exchange Commission v. U.S. Realty and Improvements Co.*, 310 U.S. 434 (1940); *Barton v. Barbour*, 104 U.S. 126 (1881); *Bank of Marin v. England*, 385 U.S. 99 (1967).

(b) payment of claims arising out of a Federal receiver's torts as priority claims. *Cowdrey v. Galveston, Houston and Henderson Ry. Co.*, 93 U.S. 352 (1876); *Hale v. Frost*, 99 U.S. 389 (1878); *McNulta v. Lochridge, supra.*

5. The decision is in conflict with the opinion of Judge Learned Hand of the Second Circuit who, in the case of *Vass v. Conron Bros. Co.*, 59 F.2d 969 (2nd Cir. 1932), stated (at p. 971) that a claim for damages arising out of the negligent operation of a business by a receiver was an expense of administration. This opinion was cited by the Judges dissenting below. Appendix C, *infra*, p. 22. The District Court for the District of Connecticut has also held that claims arising from the torts of a receiver are costs and expenses of administration in bankruptcy; In re *Progress Lektro Shave Corp.*, 35 F. Supp. 915 (D. Conn. 1940). Accordingly, the decision below has created a conflict between the Second and Third Circuits in the interpretation of the Bankruptcy Act.

6. The decision of the Court of Appeals represents a sharp departure from the accepted principles of statutory interpretation and equity jurisprudence and is in conflict with every text written on the question. See, *e.g.*, 45 Am. Jur., Receivers, §255 (1943); 45 Am. Jur., Receivers, §349 (1943); 75 C.J.S., Receivers §293(h) (1952); Clark, Receivers, §396(h) (3rd Ed. 1959); Clark, Receivers, §640.9 (3rd Ed. 1959); Collier on Bankruptcy §62.01 (14th Ed. 1964); Collier on Bankruptcy §62.03 (14th Ed. 1964); Collier on Bankruptcy §62.15 (14th Ed. 1964); Collier on Bankruptcy §64.01 (14th Ed. 1964).

CONCLUSION

For the foregoing reasons, this Petition for Writ of Certiorari should be granted.

Respectfully submitted,

By

THOMAS RAEBURN WHITE, JR.
WHITE AND WILLIAMS
Attorneys for Petitioner

CERTIFICATE OF SERVICE

STATE OF PENNSYLVANIA
COUNTY OF PHILADELPHIA ss.

I, THOMAS RAEBURN WHITE, JR., counsel for the petitioner herein, and attorney of record for the petitioners in the courts below, state that on the 2nd day of May, 1967, I served two copies of the foregoing Petition for Writ of Certiorari on the respondents, as required by Rule 33, Paragraph 1, by personally mailing said copies hereof to Messrs. Dechert, Price and Rhoads, in care of their office, 1600 Three Penn Center Plaza, Philadelphia, Pennsylvania 19102 and on the United States by mailing two copies to the Solicitor General, Department of Justice, Washington 25, D. C., and to Richard M. Roberts, Assistant Attorney General, Department of Justice, Washington, D. C. 20530, the attorney who argued the brief for the United States in the courts below.

THOMAS RAEBURN WHITE, JR.
Member of the Bar of the
United States Supreme Court

APPENDIX A

Amendment V — Capital Crimes; Double Jeopardy; Self-Incrimination; Due Process; Just Compensation for Property

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

APPENDIX B

11 U.S.C. §11 (Bankruptcy Act §2)

§11. *Creation of courts of bankruptcy and their jurisdiction.*

(a) The courts of the United States hereinbefore defined as courts of bankruptcy are created courts of bankruptcy and are invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this title, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to—

* * * * *

(2) Allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates;

* * * * * *

11 U.S.C. §102(a)(1) (Bankruptcy Act §62)

§102. *Expenses of administering estates; unauthorized sharing of fees; withholding allowances.*

(a) (1) The actual and necessary costs and expenses incurred by officers, other than refrees, in the administration of estates shall, except where other provision are made for their payment, be reported in detail under oath, and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred.

* * * * * *

11 U.S.C. §103(a)(7) (Bankruptcy Act §63(a)(7))

§103. *Debts which may be proved.*

(a) Debts of the bankrupt may be proved and allowed against his estate which are founded upon . . .

(7) the right to recover damages in any action for negligence instituted prior to and pending at the time of the filing of the petition in bankruptcy; . . .

* * * * * *

11 U.S.C. §104a)(1) (Bankruptcy Act §64(a)(1))

§104. *Debts which have priority.*

(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the costs and expenses of administration, including the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; . . .

* * * * *

APPENDIX C

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 15507

In the Matter of:

I. J. KNIGHT REALTY CORP., BANKRUPT

READING COMPANY

Appellant

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued May 5, 1966

Reargued December 8, 1966

Before STALEY, *Chief Judge* and MCLAUGHLIN, KALODNER, HASTIE, SMITH, FREEDMAN and SEITZ, *Circuit Judges*

Opinion of the Court

(Filed January 6, 1967)

By KALODNER, *Circuit Judge*

The issue presented on this appeal is whether appellant's claim, if proved, is entitled to the priority status

accorded to costs of administration by Section 64, sub.a(1) of the Bankruptcy Act.[1]

The facts are not in dispute, and have been stipulated. In substance, they are as follows:

On November 16, 1962, I. J. Knight Realty Corp. filed a petition for arrangement under Chapter XI of the Bankruptcy Act. On the same day, the District Court appointed a Receiver and authorized him to operate the debtor's business, which consisted principally in the leasing of the debtor's eight-story industrial building in Philadelphia. On January 1, 1963, this building was destroyed by a fire which spread to adjoining premises and caused damage to real and personal property of The Reading Company, appellant herein, and of others.

On April 3, 1963, appellant filed a claim for damages in the amount of $559,730.83, alleging that the receiver was negligent in permitting the fire to start and "to spread far beyond its normal confines." The claim specifically recited that it was "for administrative expenses due to the negligence of the Receiver in operation of business of the debtor." Other claimants have filed 146 additional claims, similarly grounded and similarly seeking priority status as administration expenses, totalling in excess of $3,500,000. Those claims are held in abeyance by the Referee pending the ultimate disposition of the claim now on appeal.

---

[1] "Sec. 64. Debts which have priority.

"a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the costs and expenses of administration, including the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; . . . Where an order is entered in a proceeding under any chapter of this Act directing that bankruptcy be proceeded with, the costs and expenses of administration incurred in the ensuing bankruptcy proceeding shall have priority in advance of payment of the unpaid costs and expenses of administration, including the allowances provided for in such chapter, incurred in the superceded proceeding and in the suspended bankruptcy proceeding, if any; . . ." Bankruptcy Act, §64 sub.a(1), 11 U.S.C.A. §104, sub.a(1), Sept. 25, 1962, 76 Stat. 571.

On May 14, 1963, the debtor was voluntarily adjudicated a bankrupt. A Trustee was elected, and he moved to expunge appellant's claim on the ground that it was not an administration expense under Section 64, sub.a(1) of the Bankruptcy Act.[2] The Referee expunged the claim. On petition for review, the District Court concluded that the claim was not entitled to priority as an administration expense under Section 64, sub.a(1).[3] 242 F. Supp. 337 (E.D. Pa. 1965).

We are of the opinion that the Order of the District Court should be affirmed.

The right of a claim to priority status in a Chapter XI proceeding is controlled exclusively by Section 64 of the Bankruptcy Act by virtue of the provisions of Section 302 of the Act.[4] *In the matter of Chicago Express, Incorpo-*

---

[2] The stipulation of the parties, entitled "Case Stated", is set out at 242 F. Supp. at 338-339. It appears therefrom that the Trustee will have for distribution between $630,000 and $845,000, depending on the outcome of pending litigation against fire insurance companies. The status of the instant claim becomes important particularly to the United States, which has a substantial priority claim under Section 64, sub.a(4).

[3] The District Court also concluded, as did the Referee, that appellant's claim was not provable as a general claim. 242 F. Supp. at 342. On this appeal, appellant "agrees that the claim here asserted is not provable as a general claim under §63a(7) [11 U.S.C.A. §103a(7) (1953 Supp. 1964)] of the Act. . . ." Appellant's Brief, p. 20.

[4] Chapter XI—Arrangements

"Sec. 302. The provisions of chapters I to VII, inclusive, of this Act, shall, insofar as they are not inconsistent with or in conflict with the provisions of this chapter, apply in proceedings under this chapter. For the purposes of such application, provisions relating to 'bankrupts' shall be deemed to relate also to 'debtors', and 'bankruptcy proceedings' or 'proceedings in bankruptcy' shall be deemed to include proceedings under this chapter. For the purposes of such application the date of the filing of the petition in bankruptcy shall be taken to be the date of the filing of an original petition under section 322 of this Act, and the date of adjudication shall be taken to be the date of the filing of the petition under section 321 or 322 of this Act except where an adjudication had previously been entered." July 1, 1898, c. 541, §302, as added June 22, 1938, c. 575, §1; 52 Stat. 905; 11 U.S.C.A. §702.

rated, 332 F.2d 276, 278 (2 Cir. 1964), cert. den. 379 U.S. 879; American Anthracite & Bituminous Coal Corp. v. Leonardo Arrivabene, S.A., 280 F.2d 119 (2 Cir. 1960). Manifestly, the right to priority depends upon the ability of the appellant to bring its claim within the language of the preferential classification sought. Goldie v. Cox, 130 F.2d 690 (8 Cir. 1942).

We recently expressly ruled that expenses which "are unrelated to development, preservation or distribution of the bankrupt's assets" cannot be considered "costs and expenses of administration" within the meaning of Section 64 sub.a(1) as amended in 1962. In the Matter of Connecticut Motor Lines, Inc., 336 F.2d 96 (1964).

We there said at pages 101-102:

> "Our view of the boundaries of Section 64, sub.a(1) of the Bankruptcy Act is reinforced by the latest amendment to that Section in 1962. Prior to the 1962 amendment, Section 64, sub.a(1) set forth a number of individual first priority expense items under no explicit generic label. 'Costs and expenses of administration' was one of a number of particular items enumerated in Section 64, sub.a(1). In such a posture, the Section did lend itself to a broad construction. The amendment altered the language of the Section to read as follows:
>
> "'(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) *the costs and expenses of administration, including* the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; . . . .
>
> "The impact of the amendment was to clarify the fact that Congress had considered all expenses laid out in Section 64, sub.a(1) costs and expenses of administration. The legislative history makes it clear that Con-

gress, through the amendment, wanted to underline this factor. . . .

* * * * *

"Though those enumerated costs and expenses of administration were never meant to be all inclusive, the 1962 amendment does indicate a concern that a meaningful view be had as to what is to be considered a cost and expense of administration. By explicitly structuring Section 64, sub.a(1) the Congress indicated both that all items in Section 64, sub.a(1) were costs and expenses of administration, and that the expression 'costs and expenses of administration' was not a catch-all within the first priority. With such a Congressional intent apparent, it is preferable to isolate from Section 64, sub.a(1), as falling without a meaningful view of costs and expenses of administration, those expenses which, though they can be considered *post-bankruptcy items*, are unrelated to development, preservation or distribution of the bankrupt's assets."

This touchstone guide to the direction of Section 64 sub.a(1) finds support not only in the legislative history, as shown by the Court's opinion, but also in existing authority. See, American Anthracite & Bituminous Coal Corp. v. Leonardo Arrivabene, S.A. *supra*, at 124-126; Saper v. John Viviane & Son, Inc., 258 F.2d 826 (2 Cir. 1958); Guerin v. Weil, Gotshal & Manges, 205 F.2d 302 (2 Cir. 1953). As these cases indicate, it is not every post-petition event giving rise to a cost, expense or liability which qualifies the cost, expense or liability for priority status under Section 64 sub.a(1).

This is the standard applied by the court below. We agree with it, and with its conclusion that appellant's tort claim does not fall within the restrictive language of Section 64 sub.a(1) as an expense so related to the development, preservation or distribution of estate assets as to be deemed to have been incurred in connection therewith.

Existing judicial interpretation and application of Section 64 sub.a(1) does not indicate any other result. Indeed, it is evident that the Congress knows how to assure the priorities it desires. See, In the Matter of Hudson & Manhattan Railroad Company, 178 F. Supp. 103 (S.D.N.Y. 1959), aff'd sub nom. Augus v. Stichman, 273 F.2d 707 (2 Cir. 1960); Senate Report No. 1954, accompanying the amending legislation, H.R. 5393, 1962 U.S. Code Congressional and Administrative News, pp. 2603, 2608.

Appellant seeks an application of Section 64 sub.a(1) founded upon principles, according to the authorities it cites, utilized in equity receivership proceedings. But we find no compelling persuasion in such authorities here, where we have to deal with a purposeful statutory restriction. Cf. In the Matter of the Pusey and Jones Corporation, 295 F.2d 479 (3 Cir. 1961); In the Matter of Chicago Express, Incorporated, *supra;* American Anthracite & Bituminous Coal Corp. v. Leonardo Arrivabene, S.A. *supra.*

Federal courts cannot extend the reach or sweep of a federal statute beyond its clearly defined provisions as we recently explicitly ruled in American Dredging Company v. Local 25, Marine Division, International Union of Operating Engineers, 338 F.2d 837 (1964), cert. den. 380 U.S. 935 (1965).

The purposeful statutory restriction, earlier discussed, cannot be amended by judicial legislation to accomplish the result which the minority advocates.

As we said in *American Dredging* at page 850:

> "Courts have inherent power to construe legislation and to *fashion* remedies to effectuate the legislative design but they do not have power to legislate, directly or indirectly, nor can they *amend* legislation to extend its clearly defined limits under the shelter of their power to *fashion remedies.*
>
> "The Constitution of the United States has reserved to the Congress the power to legislate. Article I, section 1 provides that 'All legislative Powers herein granted

> shall be vested in a Congress of the United States, which shall consist of a Senate and House of Representatives'.
>
> "Not even the Supreme Court of the United States can usurp the legislative power reserved to the Congress by the Constitution. The Supreme Court itself has time and again paid homage to the doctrine of the separation of powers decreed by the Constitution and declared that judicial legislation is abhorrent to, and in violation of, the Constitutional scheme."

Section 64 provides that "actual and necessary expenses of preserving the estate" are entitled to a priority. The words "actual and necessary" require that the expenses be proximately related to the preservation of the estate and that they must be reasonably anticipated as a cost of operating the business. Cf. Jopek v. New York Central R.R., 353 F.2d 778 (C.A. 3, 1965). The word "necessary" in §162(a) of the Internal Revenue Code of 1954 has been similarly construed.

This construction adequately answers the question as to whether the costs of insurance would be entitled to a priority. The insurance costs which were reasonable or which were incurred in reasonable anticipation of liability within certain limits would obviously fall within §64. Those premiums, however, which were excessive—which provided for liability far in excess of that which could be reasonably anticipated—would not be entitled to a priority and, in fact, the receiver could be surcharged for their cost.

For the reasons stated, the Order of the District Court will be affirmed.

FREEDMAN, *Circuit Judge*, dissenting.

I dissent from the majority's conclusion that §64a(1) requires the virtual immunization from tort liability of a business which is conducted by a receiver in a Chapter XI

proceeding. Congress has not given us a blueprint which yields an immediate and unequivocal answer to the question and I would therefore approach it as would men of practical business experience. I believe the conclusion to which this points is in harmony with the applicable law and accords with the equitable role of the Bankruptcy Court (§ 2 of the Bankruptcy Act. 11 U.S.C. § 11(a); see, e.g., *Bank of Marin v. England*,—U.S.—(1966); *In re Laskin*, 316 F.2d 70, 73 (3 Cir. 1963)), which applies in Chapter XI proceedings as elsewhere. See *SEC v. United States Realty & Improvement Co.*, 310 U.S. 434, 455-58 (1940).

The fundamental purpose of a Chapter XI proceeding, unlike a straight bankruptcy, is the ultimate rehabilitation of the debtor. *Nicholas v. United States*, 384 U.S. 678, 684-85 (1966); *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 603-7 (1965). The inevitable consequence of this is the continued operation of the business of the debtor and an on-going situation decisively different from the frozen rigidity of a straight bankruptcy liquidation. The reorganization court therefore applies its equitable powers to carry out this wider, business purpose.[1] Both from equitable considerations and because Congress has specifically provided that a receiver who operates the business of a debtor shall do so subject to the same requirements of law and in the same manner as if he were the debtor (28 U.S.C. § 959(b)),[2] the courts have recognized that during the

[1] See Matter of South Jersey Land Corp., 361 F.2d 610, 614-15 (3 Cir. 1966); Matter of Fleetwood Motel Corp., 335 F.2d 857, 862 (3 Cir. 1964), both Chapter X proceedings, which, despite their differences from Chapter XI, are fundamentally similar in looking to continuation of the business rather than liquidation. See SEC v. American Trailer Rentals Co., *supra*.

2 Section 959(b) reads:

"A trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof."

pendency of a Chapter XI proceeding the receiver's operation of a business should involve the risks and liabilities which normally would flow from a business operation. Such expenses therefore are entitled to payment as administrative expenses before the pre-bankruptcy claims of creditors, for whom the business is being operated as if they were stockholders. 3 *Collier on Bankruptcy* (14th ed. 1966), § 62.15, p. 1540. Thus, taxes incurred during a receivership which is established, not to wind up the business, but to foster it, have been given priority as an expense of administration. So it has been held in an equity receivership,[3] in the operation of a business in bankruptcy liquidation,[4] and in a Chapter XI proceeding.[5] These decisions have the utmost significance. They accord priority under § 64a(1) to taxes, which are not specifically listed in that section, even though the automatic accrual of such liabilities leaves no room for the rationale that priority is granted to encourage the extension of credit to the debtor.

There is no equitable reason why the claim for a tort committed by the receiver after the filing of the petition should not have the same priority which is given to a tax claim or even a contractual obligation[6] incurred after the filing of the petition. Like the operation of motor vehicles by the receiver or his employees, the shutting off of water pipes, which led to the fire, is part of an activity which may involve much profit to the estate and help to preserve the assets. It should also incur the well-known price or

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[3] Michigan v. Michigan Trust Co., 286 U.S. 334 (1932), Cardozo, J., involving state corporate franchise taxes.

[4] Boteler v. Ingels, 308 U.S. 57 (1939), involving automobile license fees and penalties.

[5] Nicholas v. United States, 384 U.S. 678 (1966), where it was said that federal income taxes and interest thereon were an administrative expense.

[6] Compare In re Delaware Hosiery Mills, Inc., 202 F.2d 951 (3 Cir. 1953), and In re Arbycraft Co., 288 F.2d 553, 557 (3 Cir. 1961), where we treated claims as administration expenses under § 64a(1), although there was no express authorization in the statute.

cost of such activities, i.e., the cost of liability insurance premiums or, absent insurance, direct responsibility for negligence as a cost and expense of preserving and managing the estate. The argument of the government that the risk of such liability would make suppliers unwilling to extend credit and secured creditors reluctant to accept an arrangement, ignores the ability to provide against that risk by insurance. To refuse to recognize claims resulting from the operation of the business is to create a substantial immunity from liability, ironically enough, at a time when it is being generally recognized that tort immunity has little justification. See, e.g., *United States v. Muniz*, 374 U.S. 150, 165-66 (1963). For it is clear that a tort claim based on post-petition activities cannot be proven as an ordinary claim. (See § 63 of the Bankruptcy Act, 11 U.S.C. § 103.) Today's decision, therefore, will discourage receivers and creditors of the debtor from approving expenditures for premiums for public liability insurance. It will not be much alleviated by the menace of surcharge for premiums which the majority now directs against receivers for misjudging the treacherous ground of "reasonable" insurance, or "reasonable anticipation of liability," or "excessive" premiums. Once again, it seems to me, contractual claims are unjustifiably exalted and the risks to which the public is exposed by torts which experience shows are an inevitable result of the operation of a business are treated as outcast. And what should a receiver do if in his wise judgment it is advantageous to the estate to continue to operate the business by following its former policy of acting as a self insurer rather than to begin to pay large premiums?

The trend of the decisions supports the view that the present claim is entitled to priority. Priority as an administrative expense has been accorded tort claims in straight bankruptcy cases.[7] It has been similarly granted in equity

[7] Vass v. Conron Bros. Co., 59 F.2d 969 (2 Cir. 1932); In re Progress Lektro Shave Corp., 35 F.Supp. 915 (D.Conn. 1940); In re Michigan Motor Specialties Co., 288 Fed. 377 (E.D. Mich. 1923).

and statutory receiverships,[8] and although it is true that equity receiverships are not governed by § 64a(1), nevertheless, with respect to administration of an estate, such receiverships are fundamentally similar to Chapter XI proceedings, a similarity which the Supreme Court has recognized in determining the scope of § 64a(1). See *Nicholas v. United States*, 384 U.S. 678, 684 n. 12 (1966). There is no reason why we should not do the same.

The three cases cited by the majority in support of its refusal to apply the equity rule, *In re Pusey & Jones Corp.*, 295 F.2d 479 (3 Cir. 1961), *In re Chicago Express, Inc.*, 332 F.2d 276 (2 Cir. 1960), cert. denied, 379 U.S. 879 (1965), and *American Anthracite & Bituminous Coal Corp. v. Leonardo Arrivabene, S.A.*, 280 F.2d 119 (2 Cir. 1960), differ significantly from this case. None of them involved tort claims, and in each of them the claimant admittedly was entitled to share with the general creditors. Moreover, neither *Pusey & Jones* nor *Chicago Express* involved claims of priority under § 64a(1) and both dealt with the application to Chapter XI proceedings of a special rule that had come to be applied in reorganizations of "public corporations" but was not a general doctrine of equity receiverships; indeed the conclusion in both cases was based on equitable considerations. *American Anthracite* dealt with the special problem of the assumption of existing contracts by the debtor in possession for which there was a history of special statutory provisions in bankruptcy.

The majority relies heavily on *In the Matter of Connecticut Motor Lines*, 336 F.2d 96 (3 Cir. 1964). We there held that tax expenses arising out of activities which occurred prior to the filing of the petition were properly allocable to the pre-petition period and therefore not en-

[8] E.g., Texas & Pacific Railway Co. v. Bloom's Adm'r., 164 U.S. 636, 642-43 (1897); Barton v. Barbour, 104 U.S. 126, 130 (1881); Bereth v. Sparks, 51 F.2d 441 (7 Cir. 1931) citing numerous cases; Anderson v. Condict, 93 Fed. 349, 354 (7 Cir. 1899); see also Valdes v. Feliciano, 267 F.2d 91, 95 (1 Cir. 1959).

titled to be treated as administrative expenses, but were included in § 64a(4). The opinion of the court stated that "it is preferable to isolate from Section 64, sub.a(1), as falling without a meaningful view of costs and expenses of administration, those expenses which, though they can be considered post-bankruptcy items, are unrelated to development, preservation or distribution of the bankrupt's assets." (p. 102) But that statement must be read in the light of the critical point, which the court emphasized, that priority would have been accorded the taxes if they had accrued after the filing of the petition, because in such case they would have been a "cost of protecting the fund". (p. 100) A tort claim similarly is entitled to priority; it is as much an expense of management or "development" of the estate as is a tax claim.[9]

Finding no expression in the statute to the contrary, but rather sufficient authority in its language to include the present claim, I would not recoil from doing so because it is based on a tort. I would follow the terse and specific dictum of Judge Learned Hand that "the liquidation of the lessee's resulting damages [from the trustee's negligence] was as much a part of the usual administration in bankruptcy, as that of the pay of accountants, custodians or other assistants, employed by the trustee." *Vass v. Conron Bros. Co.*, 59 F.2d 969, 971 (2 Cir. 1932).

Judges Smith and Seitz concur in this dissent.

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[9] Guerin v. Weil, Gotshal & Manges, 205 F.2d 302 (2 Cir. 1953), cited by the majority, does not govern here, and in any event, its disallowance of the expenses of petitioning creditors for the service of attorneys and accountants was overturned by Congress in 1962, Pub. L. 87-681. See S.Rep. No. 1954, 87th Cong., 2d Sess. (1962), 1962-2 U.S. Code, Cong. & Adm. News 2603, 2608.